

This letter discusses the distinction between a sale at retail and a sale of service. See 86 Ill. Adm. Code 130.101 et seq. and 86 Ill. Adm. Code 140.101 et seq. (This is a GIL.)

December 30, 2005

Dear Xxxxx:

This letter is in response to your letter dated January 26, 2005, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

ABC is the administrative arm of the parent company, XYZ. The tax department at ABC, of which I am employed, handles all taxing issues for the subsidiaries of XYZ. COMPANY is one of those subsidiaries.

I am writing to you for an answer on the taxability of a specific type of transaction:

BUSINESS is an operating division of COMPANY. The company has a 100 year history here in STATE. One portion of our manufacturing relates to the custom design and creation of building facades. BUSINESS is widely recognized for their designs, not limited to but including, columns, door and window adornments, parapets and belt courses. The design, drafting and creative thought behind the completed project usually represents approximately one-third of the contract price.

We currently have a customer that has requested a design from us without a promise to give us the contract for its manufacturing. The customer has defined this creative thought to be labor and therefore, non-taxable. In the past we have always billed a single contract price for the completed terra cotta pieces with the entire contract price subject to sales tax.

Please respond to the following questions:

1. If separately stated, or in a separate contract, is the design, drafting and creative thought considered non-taxable labor?
2. The pieces are manufactured in STATE and shipped via common-carrier to our customer in Illinois. Can the freight be separately stated, at the cost to us for the shipping, on the invoice for the pieces shipped and be non-taxable or must we invoice the freight separately?

Thank you for your time and consideration

DEPARTMENT'S RESPONSE

Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. If tangible personal property is not transferred, tax is not incurred. For your general information please see 86 Ill. Adm. Code Part 140 regarding sales of service and Service Occupation Tax. These regulations may be found on the Department's internet website under the heading of "Laws/Regs/Rulings."

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon how the serviceman calculates his or her liability. There are four ways that the tax can be calculated: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on the cost price if they are registered de minimis servicemen; or, (4) Use Tax on the cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the

Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

The Department's regulation on the treatment of transportation and delivery charges under the Retailers' Occupation Tax Act may be found at 86 Ill. Adm. Code 130.415. Transportation and delivery charges, also designated as shipping and handling charges, are not taxable if it can be shown that the charges are agreed to separately from the selling price of the tangible personal property sold and the charges are actually reflective of the costs of shipping. To the extent the transportation and delivery charges exceed the costs of shipping, the charges will be subject to tax.

As noted in subsection (d) of Section 130.415, if the seller and the buyer agree upon the transportation or delivery charges separately from the selling price of the tangible personal property which is sold, then the cost of the transportation or delivery service is not a part of the "selling price" of the tangible personal property which is sold, but instead is a service charge, separately contracted for, and need not be included in the figure upon which the seller computes his Retailers' Occupation Tax liability.

Delivery charges are deemed to be agreed upon separately from the selling price of the tangible personal property being sold so long as the seller requires a separate charge for delivery and so long as the charges designated as transportation or delivery or shipping and handling are actually reflective of the costs of such shipping, transportation or delivery. To the extent that such charges exceed the costs of shipping, transportation or delivery, the charges are subject to tax.

The best evidence that transportation or delivery charges were agreed to separately and apart from the selling price, is a separate and distinct contract for transportation or delivery. However, documentation which demonstrates that the purchaser had the option of taking delivery of the property, at the seller's location, for the agreed purchase price, or having delivery made by the seller for the agreed purchase price, plus an ascertained or ascertainable delivery charge, will suffice.

I hope this information is helpful. If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel

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